

GAO

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PENSION BENEFIT
GUARANTY
CORPORATION

Appearance of Improper
Influence in Certain
Contract Awards

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Chairman Grassley, Chairman Bond, and Members of the Committees:

We are pleased to be here to discuss the investigation that you asked us to undertake into alleged contracting irregularities at the Pension Benefit Guaranty Corporation (PBGC). During GAO's management review, as discussed in Ms. Bovbjerg's testimony,¹ weaknesses were identified in PBGC's procurement planning and execution processes. In particular, PBGC lacked a sound business rationale to support its approach for contracting for services at four field office locations for field benefits administration (FBA)² and may have limited competition.³ As a result of information and documentation obtained in the management review, certain contracting irregularities—regarding two contracts that appeared to involve improprieties or potentially illegal activity—were referred to us.

We investigated the facts and circumstances surrounding the award of these contracts to Integrated Management Resources Group, Inc. (IMRG). The contracts—an auditing contract and the field benefits administration contract for the FBA office in Atlanta, Georgia—were worth approximately \$40 million combined. Specifically, we investigated allegations that Bennie L. Hagans, PBGC's Director of the Insurance Operations Department, which oversees the administration of FBAs, had improperly influenced the award of these contracts to IMRG, a firm owned and operated since April 4, 1997 by Myrna Cooks. From 1987 until April 1997, Ms. Cooks was a manager and vice president of Office Specialists, Inc., a PBGC contractor; and she had overall management responsibility for Office Specialists' PBGC contracts.

In brief, Mr. Hagans' actions, as summarized in the balance of my testimony, demonstrated a lack of impartiality⁴ with respect to IMRG and created the appearance of improperly influencing the award of the two contracts we investigated. As a result, we plan on referring this matter to PBGC and the Department of Justice for them to determine what, if any, additional action may be appropriate.

¹ See *Pension Benefit Guaranty Corporation: Contracting Management Needs Improvement* (GAO/T-HEHS-00-199, Sept. 21, 2000).

² These four locations were Atlanta, Ga.; Miami, Fl.; Wilmington, Del.; and Wheeling, W.Va. The FBA offices process benefit payments for insolvent pension plans.

³ See *Pension Benefit Guaranty Corporation: Contracting Management Needs Improvement* (GAO/HEHS-00-130, Sept. 18, 2000).

⁴ *Standards for Ethical Conduct for Employees of the Executive Branch* (5 C.F.R. Part 2635 (2000)) states that "employees shall act impartially and not give preferential treatment to any private organization or individual."

Chronology of Contract Awards

Our investigation focused on two contracts awarded to IMRG. In 1997, IMRG received the first, an audit services contract. Office Specialists, Ms. Cooks' previous employer, was awarded other contracts for which IMRG had submitted proposals—contracts for FBA offices in Atlanta, Georgia; Miami, Florida; and Wheeling, West Virginia, and for in-house services. The second contract that we investigated was awarded to IMRG in 1998 after PBGC decided not to exercise its option to continue Office Specialists' Atlanta FBA contract for a second year because of poor performance.

Prior to 1997, PBGC awarded Office Specialists three sole-sourced FBA contracts for Atlanta, Miami, and Wheeling and a competed in-house services contract that included auditing services.⁵ At the time, Ms. Cooks managed these contracts for Office Specialists.

On May 30, 1997, PBGC issued a Request for Proposals (RFP) for the auditing contract with a response date of June 30, 1997. PBGC reviewed four proposals in response to the RFP, including those from IMRG and Office Specialists. Shortly thereafter, PBGC issued an RFP for the FBAs in Atlanta, Miami, and Wheeling⁶ and another RFP for the in-house services contract. Office Specialists and IMRG, among others, also submitted proposals on these RFPs.

On June 3, 1997, Mr. Hagans issued a memorandum to Mr. Robert Herting, Director of PBGC's Procurement Department, naming the three members of the individual Technical Evaluation Panels (TEP) that reviewed and scored the proposals for the auditing, FBA, and in-house services contracts. Wilmer Graham, a direct subordinate of Mr. Hagans, was placed on the TEP for the auditing contract. Mr. Hagans told us he knew that Ms. Graham was a neighbor of Ms. Cooks at the time she was on the panel. However, he denied involvement in selecting the TEP members. Ms. Graham stated that she could not recall if she had disclosed to the procurement staff that she and Ms. Cooks were neighbors and said that she did not know who had named her to the TEP. Ms. Cooks told us that she found out that Ms. Graham was on the TEP only after she had won the contract.

On July 8, 1997, the technical proposals for the auditing contract were given to PBGC's TEP. The TEP issued evaluation memoranda on August 8,

⁵ In 1997, the auditing and in-house services aspects of the contract were competed separately.

⁶ Although the RFP requested that proposals be submitted for three FBA offices as a package, PBGC ultimately awarded three separate contracts for these offices.

1997 (initial); September 22, 1997 (revised); and October 1, 1997 (final). On October 10, 1997, PBGC notified IMRG that it had been awarded the auditing contract, which had an estimated maximum value of \$13,878,025 over 5 years.

On September 9, 1997, PBGC informed Office Specialists by letter that its performance in Atlanta under the existing sole-source FBA contract was unacceptable due to high employee turnover affecting work productivity and quality, a failure to timely issue Individual Determination Letters, and mail-processing and telephone backlogs. PBGC continued to document the performance issues. Without regard to the performance issues, PBGC notified Office Specialists in October 1997 that it was awarded three FBA contracts for Atlanta, Miami, and Wheeling, as the lower of the two offerors with the highest technical scores. These 1-year contracts had 4 option years. On February 18, 1998, about 4 months after Office Specialists had been awarded the Atlanta FBA contract, PBGC issued a "cure letter" to the company advising it that PBGC considered the performance of the Atlanta FBA contract to be endangered and that failure to remedy the situation immediately could result in termination of the contract for default. This letter cited continued employee turnover, failure to hire a project manager, training problems, failure to timely issue Individual Determination Letters, overdue communications, and failure to provide timely reports to PBGC.

On May 7, 1998, Mr. Hagans issued a memorandum to Mr. Herting recommending that PBGC not exercise the option to renew Office Specialists' Atlanta FBA contract. On May 18, 1998, PBGC advised Office Specialists that it had decided not to extend the term of the Atlanta FBA contract and that the current contract would end on September 30, 1998. Subsequently, Office Specialists advised PBGC of its intention not to submit a proposal on the next Atlanta FBA contract.

On June 26, 1998, PBGC issued an RFP for the Atlanta FBA contract with a response date of July 27, 1998. This RFP resulted in four proposals, including one from IMRG. On July 27, 1998, the technical proposals for the Atlanta FBA contract were given to the assigned PBGC TEP for review and scoring. The TEP issued evaluation memorandums on July 30, 1998 (initial); August 14, 1998 (revised); and August 24, 1998 (final). On September 1, 1998, PBGC notified IMRG that it had been awarded this contract, which had an estimated maximum value of over \$25 million over 4 years (1 base year and 3 option years).

Contacts Between Mr. Hagans and Ms. Cooks Prior to Contract Awards

According to Ms. Cooks, she first met Mr. Hagans when she started managing PBGC contracts at Office Specialists, about 13 years ago. According to both Mr. Hagans and Ms. Cooks, they have a friendly working relationship. Mr. Hagans stated that he and Ms. Cooks were friends "on a business level," while Ms. Cooks stated that she is also a social friend of Mr. Hagans and has lunch or dinner with him about every 2 months.

According to an Office Specialists employee, Ms. Cooks informed several co-workers on March 11, 1997, in Atlanta that she would be leaving Office Specialists, starting her own firm, and competing on PBGC contracts. She further stated that Messrs. Hagans and Herting knew of her plans. The next day, this employee met with Mr. Hagans in Atlanta who told her that both he and Mr. Herting were aware of the above meeting at which Ms. Cooks announced her plans. This employee further stated that Mr. Hagans commented that he and Mr. Herting both "fully supported her [Ms. Cooks]" and that they had been pleased with Ms. Cooks' productivity. PBGC records reflect that on March 21, 1997, Ms. Cooks gave notice to Office Specialists that she was leaving. Ms. Cooks told us that she did not tell Mr. Hagans that she was leaving Office Specialists until April 2, 1997. Her resignation was effective April 4, 1997.

A PBGC employee, responsible for the administration of the Office Specialists' contract during the period Ms. Cooks was the company's manager, told us that over the course of several months she had repeatedly advised Mr. Hagans of persistent problems with poor contractor performance in Atlanta. She stated that Mr. Hagans had replied, "It's none of your business. Stay out of it." After Ms. Cooks resigned from Office Specialists, Mr. Hagans instructed PBGC employees to begin documenting the problems in Atlanta. This documentation resulted in the September 9, 1997, notice to Office Specialists and the subsequent cure letter.

Telephone Conversations Between Mr. Hagans and Ms. Cooks Prior to Contract Awards

Between April 4, 1997, when Ms. Cooks resigned from Office Specialists and October 10, 1997, when IMRG was awarded its first contract, 34 calls were logged from either Mr. Hagans' PBGC office telephone or his PBGC cellular telephone to Ms. Cooks' home, the location of IMRG. Ms. Cooks told us that she had received many telephone calls from Mr. Hagans during this period. She acknowledged that she had also made many telephone calls to Mr. Hagans during the same period. Regarding her many telephone conversations with Mr. Hagans after she left Office Specialists, she stated that they concerned "personnel problems" at Office Specialists. However, when asked, Ms. Cooks was unable to provide any examples or explain what she meant by this. Mr. Hagans was similarly unable to explain the

content of the many telephone conversations that he had had with Ms. Cooks. He stated that he and Ms. Cooks were friends "on a business level" and if the procurement issue came up, he always referred her to Mr. Herting. Mr. Hagans also stated that he stays out of contract issues with bidders because this is prohibited by the Federal Acquisition Regulations.⁷ We interviewed an FBA contractor who was bidding on another contract. The contractor advised us that when she contacted Mr. Hagans during the procurement, Mr. Hagans responded that he could not speak with her during the procurement process and instructed her that all future contacts should be with Mr. Herting. Ms. Cooks also denied discussing the procurement with Mr. Hagans and stated that Mr. Hagans had referred her to Mr. Herting when issues arose involving the procurement.⁸

Specifically, PBGC telephone records show that on July 10, 1997, after IMRG submitted its auditing contract proposal, two telephone calls (at 3:08 p.m. and 3:12 p.m.) were made from Mr. Hagans' office telephone to Ms. Cooks' hotel room in Atlanta. Ms. Cooks told us that she was in Atlanta to recruit Office Specialists employees for IMRG. PBGC records further indicate that Mr. Hagans traveled to Atlanta later that day. Telephone records for Ms. Cooks' hotel room indicate four calls to Mr. Hagans' hotel in Atlanta. Two of these calls were made on the evening of July 10, 1997, (at 9:17 p.m. and 9:54 p.m.); and the second two were made early on the morning of July 11, 1997, (at 5:50 a.m. and 6:33 a.m.) just before Mr. Hagans visited the Atlanta office of Office Specialists. Ms. Cooks acknowledged that during her July 1997 trip to Atlanta, she had had telephone conversations with Mr. Hagans from her hotel room. She explained that the purpose of these contacts was to request that Mr. Hagans intercede on her behalf with Office Specialists' management to stop them from interfering with their employees' discussions with Ms. Cooks about possible employment with IMRG. During his visit, Mr. Hagans met separately with both Office Specialists management and line staff. Ms. Cooks told us that Mr. Hagans resolved her problem.

⁷ The Federal Acquisition Regulations do not apply to PBGC acquisitions that are not financed with appropriated funds. However, as a matter of policy, PBGC abides by the Federal Acquisition Regulations in procuring goods and services.

⁸ Mr. Herting told us that he does not recall having any conversation with Ms. Cooks but may have had one.

Mr. Hagans' and Ms. Cooks' Conversations With IMRG's Bank Loan Officer Prior to Contract Awards

On or about August 29, 1997, after IMRG had submitted its several contract proposals but before the auditing contract was awarded on October 10, 1997, Ms. Cooks met with an officer of a Maryland bank to seek financing for IMRG. At that time, Ms. Cooks was IMRG's only employee and operated the business out of her home.

We interviewed the bank officer who processed the loan application and we reviewed the loan file that contained his contemporaneous notes and memoranda that corroborated his statements. One of these memoranda is a chronology of ongoing conversations involving this loan application. The bank officer told us, and his notes of the initial meeting reflect, that Ms. Cooks had informed him that she was competing for three contracts: an auditing contract; the combined Atlanta, Miami, and Wheeling FBA contracts; and an in-house services contract—all held by Office Specialists. He also stated that prior to approving the loan, he wanted assurances directly from the PBGC officer responsible for awarding the contracts that Ms. Cooks and IMRG would in fact be awarded the contracts she claimed to be taking over from Office Specialists. In response, Ms. Cooks provided Mr. Hagans as a reference.

The bank officer stated that he had a telephone conversation with Mr. Hagans and afterwards was convinced that Ms. Cooks' claim that she would get the contract awards was truthful. He added that this was the only conversation that he had had with Mr. Hagans. Further, PBGC telephone records show a 16-minute telephone call from Mr. Hagans' office to the bank officer on September 9, 1997. On September 15, 1997, the bank officer documented his conversations with Mr. Hagans and Ms. Cooks and began processing the \$1-million loan application for IMRG.

On October 9, 1997, Ms. Cooks notified the bank officer that IMRG had been awarded the audit contract but not the FBA or the in-house services contracts. The bank officer stated that he could not understand why she was not successful in obtaining the other contracts. In response, Ms. Cooks asserted that Office Specialists had substantially underbid IMRG. The bank officer stated and his notes reflect that on October 31, 1997, Ms. Cooks stated that Mr. Hagans had pledged to give IMRG additional work for the "savings" difference between the IMRG and the Office Specialists offers (approximately \$3 million). Ms. Cooks also told the bank officer that PBGC was taking steps to remove Office Specialists from the Atlanta FBA for nonperformance on the contract and that once this was accomplished, the contract for Atlanta would be given to IMRG. In the bank officer's notes of the initial August 29, 1997, meeting with Ms. Cooks, he noted that Ms. Cooks had informed him that a "cure letter" was about to be issued to Office Specialists on September 8, 1997. PBGC

records reflect that Office Specialists was notified of its unacceptable performance on September 9, 1997. The bank officer's memorandum prepared on November 3, 1997, to support approving the loan attributes the following statement to Ms. Cooks:

" [B]y setting Standards of Service, which the incumbent [Office Specialist] probably can't achieve, the agency can follow well-established criteria to eventually void the relationship. At that time, PBGC management has [sic] told Myrna [Ms. Cooks] her company would get the nod for the other two contracts."

The bank officer's memorandum went on to describe his "very frank discussion" with Mr. Hagans in early September about IMRG's and Ms. Cooks' abilities. It also noted Mr. Hagans as saying that "[he] campaigned continuously for [Office Specialists] removal form [sic] all three contracts in favor of Myrna [Ms. Cooks]."

This same November 3, 1997, memorandum contained another recitation that Mr. Hagans had said he "was a very big fan of Myrna's [Ms. Cooks] and politicked within the agency for her company to receive the bid."

In addition to the written notes and memoranda, the bank officer told us that Mr. Hagans also made derogatory statements about Office Specialists and made other statements to suggest that IMRG would get the PBGC contracts.

After we informed Ms. Cooks about the above facts, she claimed no knowledge of the statements attributed to her and was not aware that the bank officer had contacted Mr. Hagans even though she had used him as a reference. After we advised Mr. Hagans that we had information that he had had contact with the loan officer, he told us that he did not know he was listed as a bank reference and did not remember speaking to the bank officer. He stated that no other PBGC contractors have used him as a bank reference. He added that if he had spoken with the bank officer that it "may look wrong" and in "hindsight" it would have been "bad judgment."

Scope and Methodology

We began our investigation in July 2000. In the course of the investigation, we interviewed current and/or former employees of PBGC, IMRG, and Office Specialists. We also interviewed cognizant Maryland bank officials. In addition, we reviewed IMRG loan file records, which were subpoenaed on our behalf by the Senate Committee on Aging, and PBGC records. We conducted our investigation in accordance with quality standards for investigations as set forth by the President's Council on Integrity and Efficiency.

This concludes my prepared statement. I will be happy to respond to any questions you or other Members of the Committees may have.

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